

Michigan Film Office
Film Production Tax Credits

Audit Instructions and Expenditure Certification Guidelines

Introduction

To ensure compliance with Section 455 of the Michigan Business Tax Act, 2007 PA 36, as amended, MCL 208.1455, regarding film production tax credits, the Michigan Film Office (MFO) has developed the following instructions and guidelines for eligible production companies and independent certified public accountants to follow when requesting a post-production certificate and verifying expenditures for a film production tax credit.

Regulation

Please reference MCL 208.1455 for more information regarding the regulation and the detailed definitions of state-certified qualified productions and direct production expenditures and qualified personnel expenditures. The eligible production company and the auditor should also reference guidance issued by the MFO and the Michigan Department of Treasury with regard to MCL 208.1455 and the definition and scope of direct production expenditures and qualified personnel expenditures.

General

(a) Only actual paid expenditures clearly and demonstrably incurred in Michigan for the qualified production may be recorded and certified as direct production expenses or qualified personnel expenditures. Accounts payable, accrued charges or deferrals do not constitute direct production expenditures or qualified personnel expenditures eligible for certification.

(b) The costs to be recorded are actual costs and shall not include any mark-ups or profit additions. A qualifying "direct production expenditure" must satisfy four criteria. It must (1) be made in Michigan, (2) not be a qualified personnel expenditure, (3) be directly attributable to the production or distribution of the qualified production which is the subject of the Film Production Incentive Agreement with the MFO, and (4) be subject to taxation in Michigan. An expenditure "made in Michigan" implies the following standards: i) tangible personal property and services must be acquired by the eligible production company from a source within Michigan, and ii) services must be wholly performed within Michigan. "A source within Michigan" means that the vendor has an established physical presence in Michigan that includes both a non-temporary "bricks and mortar storefront" and at least one full time permanent employee working in Michigan. "Non-temporary" and "permanent" will generally be indicated by a presence of at least one year. The one year standard would be met with a prior presence as well as a planned future presence evidenced by a documented commitment such as entering into a one year lease for office space. The requisite physical presence of a qualified vendor business and the transaction at issue must have a nexus. Michigan physical presence unrelated to the transaction would not satisfy the criteria of "made in this state".

(c) Interest expense associated with production financing qualifies as an eligible expenditure if the expense otherwise satisfies the established requirements for a “direct production expenditure.” Only interest expense that has actually accrued and been paid by the production company will be eligible for the credit. Further, capitalized interest would probably not qualify, unless it has actually been paid.

(d) Refunds, recovery amounts from insurance claims, and credits derived from discounts, rebates, invoicing errors, purchase returns or through other methods must be credited against the production costs.

(e) Proceeds from the sale of props, equipment, production assets and other tangible personal property purchased by the eligible production company for use in the qualified production, less any gain, must be deducted from the expenditures presented in the request for a post-production certificate for the state certified qualified production.

(f) The cost report must be in US dollars and the period during which the expenditures were incurred must be disclosed.

(g) It is the eligible production company’s (the “Company”) responsibility to ensure that all of the required information is provided and conforms to the requirements and guidelines outlined in MCL 208.1455.

(h) Certification of an eligible production company’s direct production expenditures and qualified personnel expenditures in connection with a state-certified production must be performed by an auditor who is a certified public accountant and must be an independent third party as defined under generally accepted auditing standards.

(i) The auditor’s name, address, and telephone number must appear on the report.

(j) The name of the production and the unique identification number issued by the MFO must appear on the report.

(k) The auditor’s opinion must be addressed to the party that has engaged the auditor (e.g., the directors or officer of the eligible production company).

(l) The auditor’s report must be dated as of the completion of the audit fieldwork.

(m) The audit must be performed in accordance with auditing standards generally accepted in the United States and the auditor must have sufficient knowledge of accounting principles and practices generally recognized in the film, television and digital media industry.

(n) The cost of the audit report prepared for the eligible production company’s request for a certificate may not be included as an expenditure in the company’s request for a post-production certificate.

(o) A copy of the audit report prepared for the eligible production company must be submitted along with the company’s request for a post-production certificate.

Agreed-Upon Procedures

The following suggested procedures are to be performed by a certified public accountant with sufficient knowledge of accounting principles and practices generally recognized in the film, television and digital media industry. A certified public accountant engaged by an eligible production company for the purposes described herein must determine and adhere to the exact procedures required to comply with the regulation. The procedures identified below represent a suggested approach that may not be appropriate for all circumstances. In all cases, however, the certified public accountant engaged by an eligible production company must exercise its professional judgment when certifying expenditures for the tax credit.

1. Obtain and read the request for postproduction certification as prepared by the eligible production company.
2. Verify that the total qualified expenditure amounts to trial balance detail provided by the eligible production company agrees.
3. For qualified personnel expenditures as defined in MCL 208.1455(12)(j), obtain a listing by individual (individual talent or through loan-out company) of below-the-line-crew that agrees with the trial balance. To the extent practicable, review all documentation regarding the payment of compensation for each such individual and perform the following procedures set forth below. However, if a review of all documentation for all such individuals is not practicable, then the certified public accountant may use its professional judgment to select a representative sample of individuals and perform the following procedures:
 - a. Ensure that payment and compensation recorded in the eligible production company's request for postproduction certification listing for any one employee does not exceed \$2,000,000.00.
 - b. Verify that the individual was not a resident of the state of Michigan for at least 60 days before approval of the Film Production Incentive Agreement (MFO Form 002-2008) with the MFO for the eligible production.
 - c. Inspect the invoice (or equivalent documentation) to verify that the expense was clearly and demonstrably incurred in Michigan.
 - d. Obtain payment support and verify (1) the amount against trial balance detail and invoice, (2) that the company/individual paid the expense, (3) the date the expense was incurred, and (4) that withholding occurred for salaries and wages paid.
4. For direct production expenditures as defined in MCL 208.1455(12)(c)(ii), obtain a listing of all individuals (individual talent or through loan-out company) of above-the-line crew that agrees with the trial balance. To the extent practicable, review all documentation regarding the payment of compensation for each such individual and perform the following procedures set forth below. However, if a

review of all documentation for all such individuals is not practicable, then the certified public accountant may use its professional judgment to select a representative sample of individuals and perform the following procedures

- a. Ensure that payment and compensation recorded in request for postproduction certification listing for any one employee does not exceed \$2,000,000.00.
- b. Inspect the invoice (or equivalent documentation) to verify that the expense was clearly and demonstrably incurred in Michigan.
- c. Obtain payment support and verify (1) the amount against trial balance detail and invoice, (2) that the company/individual paid the expense, (3) the date the expense was incurred, and (4) that withholding occurred for any salaries and wages paid.

5. For direct production expenditures as defined in MCL 208.1455(12)(c)(i) obtain a listing that agrees with the trial balance, separated by those expenditures incurred in a “core community” as defined under section 2 of the Obsolete Property Rehabilitation Act, 2000 PA 146, MCL 125.2782. To the extent practicable, review all documentation on all such expenditures and perform the following procedures set forth below. However, if a review of all documentation for all such expenditures is not practicable, then the certified public accountant may use its professional judgment to select a representative sample of expenditures and perform the following procedures:

- a. Obtain the invoice (or equivalent documentation) and proof of payment support for each selection and verify (1) that the vendor was doing business in Michigan, (2) the amount of expense, and (3) the date the expense was incurred.
- b. Inspect the invoice (or equivalent documentation) to verify that the expense was clearly and demonstrably incurred in Michigan.
- c. Ensure the expense is properly included or excluded from the core community listing of expenditures.
- d. Verify that expenditures are appropriately recorded as direct production expenditures per MCL 208.1455(12)(c)(i) and as detailed above under General.

6. Verify that amounts reported in the request for postproduction certification are calculated at 42% of direct production expenditures for the qualified production in a core community, at 40% of direct production expenditures for the qualified production in a part of Michigan other than a core community, and at 30% for qualified personnel expenditures.